

May 13, 2013

GLORIA L. FRANKLIN, CLERK
U.S. BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA



Signed and Filed: May 11, 2013

Dennis Montali

DENNIS MONTALI
U.S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

In re) Bankruptcy Case
HOWREY LLP,) No. 11-31376DM
Debtor.) Chapter 11

MEMORANDUM DECISION ON MOTION FOR RELIEF FROM STAY

I. INTRODUCTION

Haynes and Boone, LLP ("H&B") filed a Motion For Order Confirming That The Automatic Stay Is Inapplicable, Or In The Alternative, Granting Relief From The Automatic Stay (the "Motion") on April 2, 2013. The Motion was prompted by a threatened lawsuit against H&B by Allan B. Diamond, chapter 11 trustee ("Trustee"), to recover profits earned by H&B on matters brought to it by a former member of Howrey LLP ("Debtor").

Trustee made good on his threat three days later and filed an adversary proceeding (Diamond v. Haynes and Boone, LLP, A.P. No 13-03056) (the "Adversary Proceeding") in this court. As predicted, the Trustee alleges, *inter alia*, that Debtor's waiver of the duty of departing partners to account for unfinished hourly business was a fraudulent transfer under § 548, and that H&B is

1 liable under § 550¹. Paragraph 1 of the complaint states:

2 The Trustee files this lawsuit to recover a
3 valuable asset of the Debtor's estate. After or prior
4 to Howrey's dissolution, H&B, by virtue of hiring a
5 former Howrey partner from Howrey's Washington, D.C.
6 office, has received the benefit of the revenues and
7 profits from completing Howrey's unfinished business.
8 The Trustee is entitled to recover the profits H&B has
9 obtained from Howrey's unfinished business.

10 Trustee contends that H&B is liable for profits earned on
11 Debtor's unfinished business as the entity for whose benefit the
12 transfers were made and/or the immediate or mediate transferee of
13 the initial transferees of such transfers.² More specifically, he
14 seeks to recover profits earned on two hourly matters that Richard
15 Ripley, a former partner of Debtor, brought to H&B.

16 H&B contends in its Motion that the law of the District of
17 Columbia, applicable to Debtor's partnership agreement,
18 establishes a fundamental legal principle on which the Adversary
19 Proceeding turns. That is, that Debtor's partners had no duty to
20 account to the firm for unfinished business on hourly rate
21 matters, so a partner of Debtor who joined H&B would not have a
22 duty to account for hourly rate matters handled prior to
23 dissolution.³ Thus, absent a duty to account, the waiver by

24 ¹ Unless otherwise indicated, all chapter, section and rule
25 references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1532, and
26 to the Federal Rules of Bankruptcy Procedures, Rules 1001-9037.

27 ² For a fuller explanation of the theory of Trustee's case,
28 see Greenspan v. Orrick, Herrington & Sutcliff LLP (In re Brobeck,
29 Phleger & Harrison, LLP), 408 B.R. 318 (Bankr. N.D. Cal. 2009) and
30 Heller Ehrman LLP v. Jones Day (In re Heller Ehrman LLP), 2013 WL
31 951706 (Bankr. N.D. Cal. Mar. 11, 2013).

32 ³ Much of the literature, case law and briefing about the
33 unfinished business rule divide the legal fee universe into hourly
34 rate and contingency cases. Curiously few, if any, appear to
35 address alternative billing arrangements such as fixed price legal

1 Debtor and its partners of such a duty could not be attacked as a
2 fraudulent transfer because nothing of value was transferred. H&B
3 calls this a "threshold" issue that has not been addressed by the
4 District of Columbia courts.

5 H&B wants to file a declaratory relief action against the
6 Trustee in the Superior Court of the District of Columbia (the
7 "Dec Relief Action"). It contends that the automatic stay of §
8 362(a) does not prevent it doing so. If the automatic stay does
9 apply, H&B seeks relief from stay to file and prosecute the Dec
10 Relief Action for cause, citing judicial economy and the
11 specialized knowledge and expertise of the District of Columbia
12 courts.

13 Trustee's position is that District of Columbia law applies;
14 the law there is well-settled; this court can apply that law; the
15 automatic stay applies; and relief from stay is not warranted.

16 For the reasons set forth below, the court concludes that
17 the Trustee's claims, first threatened and now asserted in the
18 Adversary Proceeding, are property of the estate protected by the
19 automatic stay. H&B's prosecution of the Dec Relief Action would
20 essentially be a defense more properly asserted and adjudicated in
21 the Adversary Proceeding. Such prosecution elsewhere would be the
22 exercise of control over property of the estate. Accordingly the
23 automatic stay applies. Further, H&B has not persuaded the court
24 that cause exists to grant relief from stay. Thus the Motion will

25 work, project based fees, success fees, blended hourly rate and
26 contingency fee engagements or other creative methods for
27 compensating attorneys. If contingency cases on one end of the
28 spectrum are subject to the rule and hourly rate matters at the
other end are not, where the dividing line is for alternative
arrangements is food for much future thought.

1 be DENIED in all respects, eliminating the need for the court to
2 consider Trustee's alternative, namely to seek injunctive relief
3 in the Adversary Proceeding prohibiting H&B from filing and
4 prosecuting the Dec Relief Action.

5 II. DISCUSSION

6 Debtor's partnership agreement recites, in part,

7 "... that all clients for legal services served by any
8 partners ... of the [Debtor] are clients of the Partnership,
9 not of any partner or employee, and that the Partnership has
10 a legitimate interest in preserving and maintaining all
11 aspects of its business, including its economically valuable
12 relationships with its clients, as well as with its partners
13 and employees. It is further expressly acknowledged and
14 agreed that all partners and employees of the [Debtor] have a
fiduciary duty to assist the [Debtor] in preserving and
protecting all aspects of its business, and no partner or
employee shall act in any way contrary to the interest of the
[Debtor] ... including the solicitation of [Debtor] clients,
partners or employees contrary to the provisions of this
Paragraph."

15 Partnership Agreement at ¶ 13.9.

16 That paragraph ends by stating it is deemed modified "to the
17 extent required by any applicable Code of Professional
18 Responsibility or other applicable professional disciplinary rules
19 or other applicable laws binding on the [Debtor]."

20 On March 9, 2011, the partners of Debtor amended the
21 Partnership Agreement to waive any rights Debtor may have to
22 profits from any unfinished business (the "Jewel Waiver") and on
23 the same date the Debtor elected to dissolve, effective March 15,
24 2011. The Jewel Waiver is the transfer Trustee contends was a
25 fraudulent transfer that he can avoid as a necessary step in
26 establishing H&B's liability under § 550.

27 The Dec Relief Action would seek to establish that the final
28 sentence of ¶ 13.9 (and the law it imports) trumps the duties

1 imposed (as to hourly rate matters) earlier in that paragraph; if
2 so, the Jewel Waiver waived nothing.

3 H&B argues that the Dec Relief Action could not have been
4 brought prior to bankruptcy, and thus did not implicate
5 § 362(a)(1). As to § 362(a)(3), H&B contends that such an action
6 would not be one to obtain possession of property of the estate or
7 to exercise control of the property of the estate. It suggests
8 that no other provision of § 362 is implicated and Trustee does
9 not contend otherwise.

10 The parties have devoted a portion of their written arguments
11 for and against the applicability of § 362(a)(1). The court sees
12 no purpose in trying to answer the somewhat philosophical question
13 of whether H&B could have sued Debtor prior to bankruptcy to have
14 a declaration that the unfinished business rule did not apply to
15 hourly rate matters in the District of Columbia. By the time of
16 Debtor's dissolution it is safe to presume that the attack on
17 Jewel Waivers as fraudulent transfers in law firm bankruptcies was
18 a well-known reality. What intelligent financially troubled law
19 firm management would do anything but concede H&B's contentions?

20 The only automatic stay issue worth addressing here is
21 whether forcing the Trustee or the Creditors Committee to defend
22 the Dec Relief Action in the District of Columbia would amount to
23 control over property of the estate. Stated otherwise, would it
24 interfere with Trustee's prosecution of the Adversary Proceeding
25 where the very same legal issue that can and no doubt will be
26 raised by H&B (and perhaps other law firm defendants in similar
27 adversary proceedings).

28 Property of the estate is a broadly defined term, and clearly

1 includes causes of action. Sierra Switchboard Co. v. Washington
2 Elec. Corp., 789 F. 2d 705 (9th Cir. 1986). Asserting what could
3 be a case-dispositive defense to such a cause of action by taking
4 the initiative in another forum improperly seeks to take control
5 over an asset of this estate. The court agrees with the reasoning
6 of the bankruptcy court in Securities Investor Protection Corp. v.
7 Bernard L. Madoff Inv. Securities, LLC (Bankr. S.D.N.Y. 2011) 460
8 B.R. 106, 113 aff'd, (S.D.N.Y. 2012) 474 B.R. 76. While Lovett v.
9 Honeywell, Inc. (In re Transportation Systems International, Inc.)
10 110 B.R. 888 (D. Minn. 1990), held that there were no § 362(a)(3)
11 implications in an action brought before the Interstate Commerce
12 Commission that would, if successful, undermine a trustee's cause
13 of action, the Madoff decision was affirmed by the District Court
14 just a year ago, without so much as a reference to Lovett.
15 Neither district court decision is binding but Madoff if much more
16 recent and far more persuasive.

17 If H&B is right, this court can apply District of Columbia
18 law in its favor in the context of the full record that would be
19 presented when the issue is raised, presumably by a motion to
20 dismiss or a motion for summary judgment. Or maybe H&B would
21 prevail in the Adversary Proceeding on some other ground.
22 Whatever the ultimate outcome, splitting the Trustee's causes of
23 action so that they are asserted here but defended elsewhere
24 interferes with and amounts to control of those causes of action.

25 In determining that the Dec Relief Action would violate the
26 automatic stay the court is not heading down a slippery slope to
27 suggest that parties sued by bankruptcy trustees or debtors in
28 possession (whether in the "home" bankruptcy court or elsewhere),

1 cannot raise their affirmative defenses. The court expects H&B to
2 do exactly that in the Adversary Proceeding. Rather, taking an
3 affirmative step to thwart the Trustee's claims in another forum
4 is what amounts to the impermissible control. The problem could
5 be exacerbated by the fact that Trustee may be suing other law
6 firms who acquired Debtor's former partners who practice in
7 jurisdictions other than the District of Columbia, and those law
8 firms may indeed seek to invoke the laws of the other
9 jurisdictions where other rules apply. This is the more
10 threatening "slippery slope" that the Trustee is entitled to avoid
11 by denial of the Motion.

12 From the foregoing the court concludes that § 362(a)(3) is
13 implicated and that prosecution of the Dec Relief Action would
14 violate that subsection and be void.

15 The remaining issue is whether H&B should have relief from
16 the automatic stay to proceed with the Dec Relief Action. The law
17 is well settled that granting or denying relief from stay is a
18 matter of the court's sound discretion, and frequently involves
19 consideration of numerous factors. In re Kronemeyer, 405 B.R. 915
20 (9th Cir. BAP 2009). Those factors include the following:

- 21 1. Will relief result in partial or complete resolution of
22 the issues?
- 23 2. Is there a lack of any connection with or interference
24 with the bankruptcy case?
- 25 3. Does the foreign proceeding involve the debtor as a
26 fiduciary?
- 27 4. Has a special tribunal been established to hear the
28 particular cause of action and does that tribunal have the

1 expertise to hear such cases?

2 5. Has the debtor's insurance carrier has assumed financial
3 responsibility?

4 6. Does the action involve third parties and the debtor
5 functions only as a bailee or conduit?

6 7. Would litigation in the other forum prejudice the
7 interests of other creditors, the creditors committee and other
8 parties?

9 8. Would the judgment claim arising from the foreign action
10 be subject to equitable subordination?

11 9. Would success in the nonbankruptcy forum result in a lien
12 avoidable under the bankruptcy code?

13 10. Would the interests of judicial economy and expeditious
14 and economical determination of litigation be achieved?

15 11. Have the foreign proceedings progressed to where the
16 parties have prepared for trial?

17 12. What is the impact of the stay on the parties and the
18 "balance of hurt"?

19 Truebro, Inc. v. Plumberex Specialties Products, Inc. (In re
20 Plumberex Specialites Products, Inc.), 311 B.R. 551 (Bankr. C.D.
21 Cal. 2004), citing In re Curtis, 40 B.R. 795 (Bankr. D. Utah
22 1984).

23 Factors 5, 6, 8 and 9 have no relevance here and will not be
24 considered. The court has considered the remaining eight factors
25 and nearly all tip either heavily or somewhat in favor of the
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1 Trustee.⁴

2 Factor 1 weighs slightly in favor of the Trustee. If H&B
3 prevailed in the Dec Relief Action it would still have to defend
4 the Adversary Proceeding, even though the defense may be
5 significantly enhanced by such a favorable outcome. But if H&B
6 lost the Dec Relief Action, the Adversary Proceeding would still
7 have to be tried to completion.

8 Factor 2 weighs heavily in favor of the Trustee in that, for
9 the reasons stated previously, prosecution would clearly have an
10 impact on the bankruptcy case, the Adversary Proceeding and other
11 adversary proceedings Trustee may file.

12 Factor 3 weighs slightly in favor of the Trustee because he
13 is a fiduciary, prosecuting these claims against H&B and others
14 for the benefit of the creditors of this bankruptcy estate.

15 Factor 4 weighs in favor of H&B because, although the
16 District of Columbia Superior Court is not a specialized tribunal,
17 it clearly has expertise to construe the laws of the District.
18 But this factor weighs only slightly in favor of H&B because
19 bankruptcy courts apply the law of other jurisdictions all the
20 time and that system and the subsequent appellate scheme works.
21 The fact that the issues presented here may deal with law

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23 ⁴ Considering applicable factors is part of the exercise of
24 discretion, not a simple tally. Here is what one court said about
lists of factors (there relating to abstention):

25 Although the bankruptcy court should consider all twelve
26 factors, one should not be beguiled into a false sense that a head
27 count will yield the answer with mathematical certainty. Rather,
the list serves to provide an intellectual matrix to guide the
judge who considers abstention and to enable a reviewing court to
ascertain whether there has been an abuse of discretion.

28 In re Franklin, 179 B.R. 913, 928 (Bankr. E.D. Cal. 1995) .

1 professionals and their ethics does not change that obvious fact.

2 Factor 7 weighs in favor of the Trustee and the estate. Even
3 though H&B has agreed that the Creditors Committee could
4 participate in the Dec Relief Action, it would prejudice creditors
5 of this estate to have to prosecute this action in two different
6 ends of the country notwithstanding the fact that the creditors
7 committee's counsel is physically located near the District of
8 Columbia.

9 Factor 10 weighs in favor of the Trustee in that the
10 Adversary Proceeding might very well be disposed of by a summary
11 judgment in favor H&B if it is correct on the inapplicability of
12 the unfinished business doctrine to hourly rate matters in the
13 District of Columbia. Further, a disposition by this court could
14 be the subject of a direct appeal to the Ninth Circuit under 28
15 U.S.C. § 158(d)(2) and while that may appear to be more cumbersome
16 then the appellate process directly in the District of Columbia,
17 the outcome there might implicate Factor 1 that this court has
18 already determined weighs in favor of the Trustee.

19 Factor 11 weighs heavily in favor of the Trustee since the
20 Dec Relief Action has not been filed.

21 Factor 12 weighs in favor of the Trustee for a variety of
22 reasons already stated, but also because the Trustee's choice of
23 forum is entitled to some deference.

24 From all the foregoing the court is satisfied that H&B has
25 not presented adequate cause to entitle it to relief from stay.
26 Accordingly, the Motion will be denied in all respects.

27 The court is entering an order to that effect concurrently
28 with the issuance of this Memorandum Decision.

1 **END OF MEMORANDUM DECISION**

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